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SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-70836; File No. SR-EDGX-2013-40)

November 8, 2013

Self-Regulatory Organizations; EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend EDGX Rule 3.5 (Advertising Practices) and to Repeal Rule 3.20 (Initial or Partial Payments) to Conform with the Rules of the Financial Industry Regulatory Authority, Inc.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 28, 2013, EDGX Exchange, Inc. (“Exchange” or “EDGX”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which items have been substantially prepared by the Exchange. The Exchange has designated the proposed rule change as constituting a “non-controversial” rule change under Exchange Act Rule 19b-4(f)(6), which renders the proposal effective upon receipt of this filing by the Commission.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend EDGX Rule 3.5 (Advertising Practices) and repeal EDGX Rule 3.20 (Initial or Partial Payments) to conform with the rules of the Financial Industry Regulatory Authority, Inc. (“FINRA”) for purposes of an agreement between the Exchange and

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 17 CFR 240.19b-4(f)(6).

FINRA pursuant to Exchange Act Rule 17d-2.<sup>4</sup> The text of the proposed rule change is available on the Exchange's website at <http://www.directedge.com>, at the Exchange's principal office, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

Pursuant to Exchange Act Rule 17d-2,<sup>5</sup> the Exchange and FINRA entered into an agreement to allocate regulatory responsibility for common rules ("17d-2 Agreement"). The 17d-2 Agreement covers common members of the Exchange and FINRA ("Common Members") and allocates to FINRA regulatory responsibility, with respect to Common Members, for the following: (i) examination of Common Members for compliance with federal securities laws, rules and regulations and rules of the Exchange that the Exchange has certified as identical or substantially similar to FINRA rules; (ii) investigation of Common Members for violations of federal securities laws, rules and regulations, and the rules of the Exchange that the Exchange has certified as identical or substantially identical to FINRA rules; and (iii) enforcement of

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<sup>4</sup> 17 CFR 240.17d-2.

<sup>5</sup> Id.

compliance by Common Members with the federal securities laws, rules and regulations, and the rules of the Exchange that the Exchange has certified as identical or substantially similar to FINRA rules.

The 17d-2 Agreement included a certification by the Exchange that states that the requirements contained in certain Exchange rules are identical to, or substantially similar to, certain FINRA rules that have been identified as comparable. To conform with comparable FINRA rules for purposes of the 17d-2 Agreement, the Exchange proposes to: (i) amend EDGX Rule 3.5 (Advertising Practices) and (ii) repeal EDGX Rule 3.20 (Initial or Partial Payments).

#### EDGX Rule 3.5 (Advertising Practices)

The Exchange proposes to delete the current text of Rule 3.5 and adopt text that would require Exchange members to comply with FINRA Rule 2210 as if such Rule were part of the Exchange's rules and to rename the rule "Communications with the Public."<sup>6</sup> The proposed rule text is substantially the same as Rule 2210(a) of the Nasdaq Stock Market LLC ("Nasdaq"), which was approved by the Commission.<sup>7</sup>

Currently, Exchange Rule 3.5(d) and (f) are excluded from the 17d-2 Agreement because they are not identical to, or substantially similar to, certain FINRA rules. First, Exchange Rule 3.5(d) requires that advertising and sales literature be pre-approved and signed or initialed by a supervisor while FINRA Rule 2210(b) only requires supervisory pre-approval for retail communication, and imposes different supervisory review standards for institutional

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<sup>6</sup> The Exchange does not propose to require that its members comply with subparagraph (c) of FINRA Rule 2210. FINRA Rule 2210(c) generally requires that FINRA members file certain communications with FINRA. The Exchange believes that it is inappropriate for its rules to require its members to file certain communications with FINRA as such filing requirements under FINRA rules are between FINRA and its members.

<sup>7</sup> See Exchange Act Release No. 58069 (Jun. 30, 2008), 73 FR 39360 (Jul. 9, 2008) (Notice of Filing and Immediate Effectiveness).

communication, and correspondence. Second, Rule 3.5(f) and FINRA Rule 2210(d)(6) contain different content requirements for testimonials. Exchange Rule 3.5(d) and (f) were, therefore, excluded from the 17d-2 Agreement because their requirements were not identical or substantially similar to those required under FINRA Rule 2210(b) and (d)(6) respectively. To harmonize its rules with FINRA, the Exchange proposes to delete the current text of Rule 3.5 and adopt text that would require its members to comply with FINRA Rule 2210 as if it was part of the Exchange's rules so that Rule 3.5 can be incorporated into the 17d-2 Agreement in its entirety.

The Exchange believes that these changes would help to avoid confusion among its members that are also FINRA members by further aligning the Exchange Rule 3.5 with FINRA Rule 2210. The proposed changes to Rule 3.5 are designed to enable the Exchange to incorporate Rule 3.5 into the 17d-2 Agreement, further reducing duplicative regulation of Exchange members that are also FINRA members.

#### Summary of FINRA Rule 2210

FINRA Rule 2210 generally sets forth the content, filing, supervisory review, and record retention for FINRA members' communications with the public. A summary of FINRA Rule 2210 is below. A complete description of FINRA Rule 2210 is provided in FINRA's Regulatory Notice 12-29.<sup>8</sup>

FINRA Rule 2210 divides a member's communications with the public into the following three categories:

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<sup>8</sup> See FINRA Regulatory Notice 12-29 (June 2012) available at [http://finra.complinet.com/net\\_file\\_store/new\\_rulebooks/f/i/FINRANotice12\\_29.pdf](http://finra.complinet.com/net_file_store/new_rulebooks/f/i/FINRANotice12_29.pdf).

- Institutional communication. FINRA Rule 2210(a)(3) defines “institutional communication” as “any written (including electronic) communication that is distributed or made available only to institutional investors, but does not include a member’s internal communications.”
- Retail communication. FINRA Rule 2210(a)(5) defines “retail communication” as “any written (including electronic) communication that is distributed or made available to more than 25 retail investors within any 30-day calendar period.” “Retail investor” includes any person other than an institutional investor, regardless of whether the person has an account with the firm. Communications that are considered advertisements and sales literature fall under the definition of “retail communication.”
- Correspondence. FINRA Rule 2210(a)(2) defines “correspondence” as “any written (including electronic) communication that is distributed or made available to fewer than 25 retail investors within any 30-day calendar period.”

Supervisory Review. To comply with FINRA Rules 2210(b)’s supervisory requirements, Common Members must obtain supervisory pre-approval of all retail communications, while institutional communications and correspondence would be subject to supervisory review, but not pre-approval.

Under FINRA Rule 2210(b)(1), all retail communications must be approved by a supervisor prior to their first use or filing with FINRA under FINRA Rule 2210(c). FINRA’s Rule 2210(b)(1)’s supervisory requirements do not apply to a retail communication if, at the time that a member intends to publish or distribute it: (i) another member has filed it with FINRA and has received a letter from FINRA stating that it appears to be consistent with applicable standards; and (ii) the member has not materially altered it and will not use it in a manner that is

inconsistent with the conditions of FINRA's letter. The rule's supervisory review requirements also do not apply to the following retail communications, provided that the member supervises and reviews such communications in the same manner as required for supervising and reviewing correspondence pursuant to NASD Rule 3010(d): (i) any retail communication that is excepted from the definition of "research report" pursuant to NASD Rule 2711(a)(9)(A), unless the communication makes any financial or investment recommendation; (ii) any retail communication that is posted on an online interactive electronic forum; and (iii) any retail communication that does not make any financial or investment recommendation or otherwise promote a product or service of the member.

For institutional communications, FINRA Rule 2210(b)(3) requires a member to establish written procedures that are appropriate to its business, size, structure, and customers for the review by an appropriately qualified registered principal of institutional communications used by the member and its associated persons. Such procedures must be reasonably designed to ensure that institutional communications comply with applicable standards. When such procedures do not require review of all institutional communications prior to their first use or distribution, they must include provisions for: (i) the education and training of associated persons as to the firm's procedures governing institutional communications; (ii) the documentation of such education and training; and (iii) surveillance and follow-up to ensure that such procedures are implemented and adhered to. A member must maintain and make available to FINRA upon request evidence that these supervisory procedures have been implemented and carried out.

FINRA Rule 2210(b)(2) states that correspondence is subject to the supervision and review requirements of NASD Rule 3010(d). Under NASD Rule 3010(d)(2), each member shall develop written procedures that are appropriate to its business, size, structure, and customers for

the review of incoming and outgoing written (i.e., non-electronic) and electronic correspondence with the public relating to its investment banking or securities business. These written procedures should include procedures: (i) to review incoming, written correspondence directed to registered representatives and related to the member's investment banking or securities business; (ii) to properly identify and handle customer complaints; and (iii) to ensure that customer funds and securities are handled in accordance with firm procedures. When such procedures do not require review of all correspondence prior to their first use or distribution, they must include provisions for: (i) the education and training of associated persons as to the firm's procedures governing correspondence; (ii) the documentation of such education and training; and (iii) surveillance and follow-up to ensure that such procedures are implemented and adhered to.

Record Retention. Under FINRA Rule 2210(b)(4)(A), members must maintain all retail communications and institutional communications for the retention period required by Exchange Act Rule 17a-4(b) and in a format and media that comply with Exchange Act Rule 17a-4. The records must include:

- a copy of the communication and the dates of first and (if applicable) last use of such communication;
- the name of any registered principal who approved the communication and the date that approval was given;
- in the case of a retail communication or an institutional communication that is not approved prior to first use by a registered principal, the name of the person who prepared or distributed the communication;
- information concerning the source of any statistical table, chart, graph or other illustration used in the communication; and

- for any retail communication for which principal approval is not required pursuant to FINRA Rule 2210(b)(1)(C), the name of the member that filed the retail communication with the Department, and a copy of the corresponding review letter from the Department.

Filing Requirements. Like Nasdaq Rule 2210(a), Exchange Rule 3.5 would expressly state that Exchange members would not be required to comply with FINRA Rule 2210(c).

FINRA Rule 2210(c) generally requires FINRA members to file certain retail communications with FINRA prior to their first use. Exchange members who are also FINRA members would continue to be subject to FINRA Rule 2210(c).

Content Standards. FINRA Rule 2210(d) sets forth general content standards for all communications. More specifically, all member communications must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluating the facts in regard to any particular security or type of security, industry, or service. No member may omit any material fact or qualification if the omission, in light of the context of the material presented, would cause the communication to be misleading. No member may make any false, exaggerated, unwarranted, promissory or misleading statement or claim in any communication. No member may publish, circulate or distribute any communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading. Information may be placed in a legend or footnote only in the event that such placement would not inhibit an investor's understanding of the communication. Members must ensure that statements are clear and not misleading within the context in which they are made, and that they provide balanced treatment of risks and potential benefits. Communications must be consistent with the risks of fluctuating prices and the uncertainty of dividends, rates of return and yield inherent to investments. Members must consider the nature



of the audience to which the communication will be directed and must provide details and explanations appropriate to the audience.

Communications may also not predict or project performance, imply that past performance will recur or make any exaggerated or unwarranted claim, opinion or forecast; provided, however, communications may include: (i) a hypothetical illustration of mathematical principles, provided that it does not predict or project the performance of an investment or investment strategy; (ii) an investment analysis tool, or a written report produced by an investment analysis tool, that meets the requirements of FINRA Rule 2214; and (iii) a price target contained in a research report on debt or equity securities, provided that the price target has a reasonable basis, the report discloses the valuation methods used to determine the price target, and the price target is accompanied by disclosure concerning the risks that may impede achievement of the price target.

Testimonials. FINRA Rule 2210(d)(6) requires that: (i) if a testimonial in a communication includes a technical aspect of investing, the person making the testimonial must have the knowledge and expertise to form a valid opinion; and (ii) retail communications or correspondence providing any testimonial concerning the investment advice or investment performance of a member or its products must also prominently disclose that the testimonial: (a) may not be representative of the experience of other customers; (b) is no guarantee of future performance or success; and (c) is a paid testimonial, if more than \$100 in value has been paid.

Recommendations. FINRA Rule 2210(d)(7)(A) requires that retail communications that include a recommendation of securities must have a reasonable basis for the recommendation and must disclose, if applicable, the following: (i) that at the time the communication was published or distributed, the member was making a market in the security being recommended,

or in the underlying security if the recommended security is an option or security future, or that the member or associated persons will sell to or buy from customers on a principal basis; (ii) that the member or any associated person that is directly and materially involved in the preparation of the content of the communication has a financial interest in any of the securities of the issuer whose securities are recommended, and the nature of the financial interest (including, without limitation, whether it consists of any option, right, warrant, future, long or short position), unless the extent of the financial interest is nominal; and (iii) that the member was manager or co-manager of a public offering of any securities of the issuer whose securities are recommended within the past 12 months. Members must provide, or offer to furnish upon request, available investment information supporting the recommendation. When a member recommends a corporate equity security, the member must provide the price at the time the recommendation is made.

Retail communication or correspondence may not refer, directly or indirectly, to past specific recommendations of the member that were or would have been profitable to any person; provided, however, that a retail communication or correspondence may set out or offer to furnish a list of all recommendations as to the same type, kind, grade or classification of securities made by the member within the immediately preceding period of not less than one year, if the communication or list: (i) states the name of each such security recommended, the date and nature of each such recommendation (e.g., whether to buy, sell or hold), the market price at that time, the price at which the recommendation was to be acted upon, and the market price of each such security as of the most recent practicable date; and (ii) contains the following cautionary legend, which must appear prominently within the communication or list: “it should not be

assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list.”

Rule 3.20 (Initial or Partial Payments)

The Exchange also proposes to delete Exchange Rule 3.20. In January 2010, FINRA repealed NASD Rule 2450 (Initial or Partial Payments) and does not currently include a comparable rule in its rulebook.<sup>9</sup> Like NASD Rule 2450, Exchange Rule 3.20 prohibits any arrangement whereby the customer of an Exchange member submits partial or installment payments for the purchase of a security with the following exceptions: (i) if a member is acting as agent or broker in such transaction, it must immediately make an actual purchase of the security for the account of the customer, and immediately take possession or control of the security and maintain possession or control of the security as long as the member is under the obligation to deliver the security to the customer; (ii) if a member is acting as principal in such transaction, it must, at the time of the transaction, own such security and maintain possession or control of the security as long as the member is under the obligation to deliver the security to the customer; and (iii) if applicable to the member, the provisions of Regulation T<sup>10</sup> of the Federal Reserve Board are satisfied. Rule 3.20 also prohibits a member, whether acting as principal or agent, in connection with any installment or partial sales transaction, from making any agreement with a customer whereby the member would be allowed to pledge or hypothecate any security involved in such transaction for any amount in excess of the indebtedness of the customer to such member.

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<sup>9</sup> See Exchange Act Release No. 61542 (Feb. 18, 2010), 75 FR 8768 (Feb. 25, 2010) (Order approving proposal to repeal NASD Rule 2450).

<sup>10</sup> Federal Reserve Board, Regulation T (Credit by Brokers and Dealers), 12 CFR 220 et seq.

The Exchange proposes to repeal Exchange Rule 3.20 in light of the explicit provisions in Regulation T requiring the deposit of sufficient funds within the specified payment period. Specifically, Section 220.8 of Regulation T permits the purchase of a security in the cash account predicated on either: (i) there being sufficient funds in the account; or (ii) the member accepts in good faith the customer's agreement that full cash payment will be made.<sup>11</sup> The rule further stipulates that payment must be made within a specified payment period.<sup>12</sup> Regulation T also allows the purchase of a security in a margin account, whereby a customer must deposit an initial requirement, based upon the amount of the transaction, within the specified payment period.

The Exchange also believes the hypothecation prohibition in Exchange Rule 3.20 would no longer be relevant because it is predicated on a partial or installment payment under the rule. The Exchange notes that, notwithstanding the repeal of Rule 3.20, members would still be required to comply with all applicable federal securities laws, including Regulation T.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Exchange Act Section 6(b)(5),<sup>13</sup> which requires, among other things, that the Exchange's rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system. The Exchange believes that the proposed rule change would

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<sup>11</sup> See Section 220.8(a)(1) of Regulation T.

<sup>12</sup> According to Section 220.2 of Regulation T, payment period means the number of business days in the standard securities settlement cycle in the United States, as defined in Exchange Act Rule 15c6-1(a) (17 CFR 240.15c6-1(a)), plus two business days.

<sup>13</sup> 15 U.S.C. 78f(b)(5).

further these requirements by eliminating duplicative and unnecessary rules and advancing the development of a more efficient and effective Exchange rulebook. The Exchange believes that the proposed rule change would provide greater harmonization between the Exchange and FINRA rules of similar purpose, resulting in greater uniformity and less burdensome and more efficient regulatory compliance. As such, the proposed rule change would foster cooperation and coordination with persons engaged in facilitating transactions in securities and would remove impediments to and perfect the mechanism of a free and open market and a national market system.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act. The Exchange believes that the proposed rule change is not designed to address any competitive issues but rather to provide greater harmonization among similar Exchange and FINRA rules, resulting in less burdensome and more efficient regulatory compliance for Common Members and facilitating FINRA's performance of its regulatory functions under the 17d-2 Agreement.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The Exchange has neither solicited nor received written comments on the proposed rule change.

### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The Exchange filed the proposed rule change pursuant to Exchange Act Section 19(b)(3)(A)<sup>14</sup> and Rule 19b-4(f)(6)<sup>15</sup> thereunder. Because the proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days after the date of the filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Exchange Act Section 19(b)(3)(A) and Rule 19b-4(f)(6) thereunder.<sup>16</sup>

A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative for 30 days after the date of filing. Pursuant to Rule 19b-4(f)(6)(iii), however, the Commission may designate a shorter time if such action is consistent with the protection of investors and the public interest.<sup>17</sup> The Exchange has asked the Commission to waive the 30-day operative delay so that the proposal may become operative immediately upon filing.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because it will allow the Exchange to immediately conform its rules to corresponding FINRA rules. This will ensure that such EDGX rules will continue to be covered by the existing 17d-2 Agreement between the Exchange and FINRA. As noted by the Exchange, amending EDGX Rule 3.5 would harmonize Exchange and FINRA rules

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<sup>14</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>15</sup> See supra note 3.

<sup>16</sup> Exchange Act Rule 19b-4(f)(6) also requires the Exchange to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange satisfied this requirement.

<sup>17</sup> 17 CFR 240.19b-4(f)(6)(iii).

of similar purpose reducing duplicative regulation of Common Members. In addition, the Commission believes that the repeal of Rule 3.20 would eliminate an unnecessary rule from the Exchange's rulebook. Accordingly, the Commission hereby grants the Exchange's request and waives the 30-day operative delay.<sup>18</sup>

At any time within sixty (60) days of the filing of such proposed rule change, the Commission may summarily temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Exchange Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-EDGX-2013-40 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-EDGX-2013-40. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your

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<sup>18</sup> For purposes of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition and capital formation. See 15 U.S.C. 78c(f).

comments more efficiently, please use only one method. The Commission will post all comments on the Commission's website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.



All submissions should refer to File Number SR-EDGX-2013-40 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>19</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>19</sup> 17 CFR 200.30-3(a)(12).